COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0336-02
Bill No.: Truly Agreed To and Finally Passed SCS for SB 19
Subject: Corporations; Revenue Dept; Taxation and Revenue - General
Type: Original
Date: May 3, 2011

Bill Summary: Would limit a corporation's franchise tax liability to the previous year's tax or to the corporation's first year franchise tax in the case of a new corporation, and would phase out the corporate franchise tax over five years.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
General Revenue *	$0	(Could Exceed $16,554,054)	(Could exceed $35,000,000)
Total Estimated Net Effect on General Revenue Fund *	**$0**	**(Could exceed $16,554,054**	**(Could exceed $35,000,000)**

* Includes unknown estimated future revenue foregone.

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 9 pages.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on FTE	**0**	**0**	**0**

☒ Estimated Total Net Effect on All funds expected to exceed $100,000 savings or (cost).

☐ Estimated Net Effect on General Revenue Fund expected to exceed $100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Department of Revenue** (DOR) assume this proposal would change the corporate franchise and bank franchise tax rates and would eventually phase out the tax, which would create a negative impact to total state revenue.

Between January 1, 2010 and December 31, 2011, the annual franchise tax would be 1/30th of one percent of the taxable entity's outstanding shares and surplus, if they exceed $10.0 million.

For 2012 the rate would be 1/37th of one percent, for 2013 the rate would be 1/50th of one percent, for 2014 the rate would be 1/75nd of one percent, for 2015 the rate would be 1/150th of one percent, and for tax years beginning on or after January 01, 2016, no franchise tax would be imposed.

Assets levels reported for corporate franchise tax filers that have assets greater than $10 million have increased at a rate of 6.23% per year since 2002. The following table reflects the anticipated reduction in corporation franchise tax, if asset levels continue to increase as the tax is phased out.

ASSUMPTION (continued)

Franchise Tax

Year	Tax in millions	Expected Reduction in millions
2011	$88.1	$5.5
2012	$80.6	$18.8
2013	$63.4	$42.2
2014	$44.9	$67.3
2015	$23.8	$95.4
2016	$0.0	$126.6

The table above is based on tax years, but the majority of corporations file and pay their franchise tax by April of each tax year. Therefore, the 2012 reduction would impact FY 2012. Since the bill would take effect after the close of FY 2011, and since corporations can amend their 2011 returns, the tax year 2011 reduction would impact FY 2012, bringing the total potential impact in reduced revenues for FY 2012 to $24.3 million.

DOR officials also provided actual total franchise tax collections of $87.5 million for the year ended June 30, 2010.

DOR officials did not indicate any administrative impact to their organization, but they stated that the Department and the Office of Administration, Information Technology Services Division (ITSD-DOR) would need to make programming changes to various DOR systems. DOR officials estimated the IT portion of the fiscal impact at $26,712, based on 1,008 hours of programming.

Oversight assumes that ITSD-DOR is provided with core funding to handle a certain amount of activity each year, and assumes ITSD-DOR could absorb the costs related to this proposal. If multiple bills pass which require additional staffing and duties at substantial costs, ITSD-DOR could request funding through the appropriation process.

ASSUMPTION (continued)

Officials from the **University of Missouri, Economic and Policy Analysis Research Center** (EPARC) assume that if enacted, this legislation would gradually phase-out the corporate franchise tax over a five year period.

For the tax year 2011, the rate would remain at one-thirtieth of one percent and the threshold amount would remain at $10 million dollars. For 2012, the rate would be reduced to one thirty-seventh of one percent. For the tax year 2013, the rate would be reduced to one fiftieth of one percent. For the tax year 2014, the rate would be reduced to one seventy-fifth of one percent. For the tax year 2015, the rate would decrease to one hundred-fiftieth of one percent. Effective January 1, 2016, no corporate franchise tax would be imposed.

The following estimates were generated using corporate tax data from 2008. The table reports the potential total franchise tax for corporations with assets greater than $10 million in Missouri for the years 2011 through 2016 if this proposal was implemented.

Year	Franchise Tax Rate	Franchise Tax Due	Reduction in Franchise Tax
2011	1/30 of 1%	$76,703,328	$0
2012	1/37 of 1%	$64,401,130	$12,302,198
2013	1/50 of 1%	$49,349,749	$27,353,579
2014	1/75 of 1%	$34,068,533	$42,634,795
2015	1/150 of 1%	$17,639,375	$59,063,953
2016	None	$0	$76,703,328

ASSUMPTION (continued)

EPARC officials assumed that the proposed franchise tax cap would have no impact on the estimated figures shown above. EPARC officials stated that the rate of reduction in the tax rate exceeds their estimated asset growth rate for existing corporations.

Regarding new corporations, the impact would depend on the number and the tax base associated with each new corporation. It should be noted that the forecast for the tax base of new corporations is shifted to zero. For new corporations entering Missouri during or after 2011, there is an incentive to legally report no tax base. Since their future tax liabilities are pinned to the first year's franchise tax bill, the entrants into the Missouri market can incorporate, report zero assets in the state for the first year, and have no franchise tax liability in the first year of incorporation. In all years after the first tax reporting period, their tax liability would also be zero.

Officials from the **Office of Administration, Division of Budget and Planning** (BAP) assume this proposal would not result in additional costs or savings to on their organization. BAP officials stated that this proposal would phase out franchise taxes over five years, starting with tax years beginning on or after 1/1/12, which could impact franchise tax payments beginning as early as April 2012. In addition, the proposal would cap franchise tax liability at tax year 2010 levels.

BAP assumes General and Total State Revenues would be reduced beginning in Fiscal Year 2012, deferring to the DOR for estimated reductions.

ASSUMPTION (continued)

Oversight assumes an estimate of the revenue reduction for this proposal can be based on the Department of Revenue's reported 2010 collections, as shown in the following chart.

Rate reduction estimate

Year	Franchise Tax Rate	Franchise Tax Due	Reduction in Franchise Tax
2011	1/30 of 1%	$87,500,000	$0
2012	1/37 of 1%	$70,945,946	$16,554,054
2013	1/50 of 1%	$52,500,000	$35,000,000
2014	1/75 of 1%	$35,000,000	$52,500,000
2015	1/150 of 1%	$17,500,000	$70,000,000
2016	None	$0	$87,500,000

Tax liability cap estimate

These provisions would limit a corporation's annual franchise tax liability for all years beginning on or after January 1, 2011 to the amount of the corporation's franchise tax liability for the year ended December 31, 2010. If the corporation was not in existence in 2010, that corporation's franchise tax liability could not exceed its franchise tax liability for its first full year of business in Missouri.

Oversight notes that franchise tax collections fluctuate from year to year, and assumes that this proposal could result in a reduction of revenues in the future if the DOR estimate of future taxable capital and surplus is realized. For fiscal note purposes only, Oversight will indicate an unknown revenue reduction for the General Revenue Fund for that foregone potential future revenue.

Oversight assumes that corporations with tax years beginning in January, 2011 would file tax returns in January, 2013 (FY 2013) for those tax years.

FISCAL IMPACT - State Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
GENERAL REVENUE FUND			
Revenue reduction - franchise tax phase-out	$0	($16,554,054)	($35,000,000)
Reduction in future revenue - limitation on franchise tax increases *	$0	(Unknown)	(Unknown)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	**$0**	**(Could exceed $16,554,054)**	**(Could exceed $35,000,000)**

* Estimated future revenue foregone.

FISCAL IMPACT - Local Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
	$0	**$0**	**$0**

FISCAL IMPACT - Small Business

This proposal would impact those small businesses which are currently subject to the corporate franchise tax.

FISCAL DESCRIPTION

The proposed legislation would limit a corporation's franchise tax liability to the previous year's tax or to the corporation's first year franchise tax in the case of a new corporation, and would phase out the corporate franchise tax over five years.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration
Division of Budget and Plannning
Department of Revenue
University of Missouri - Economic and Policy Analysis Research Center

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